

CITY OF LOS ANGELES, CALIFORNIA
AUDIT OBSERVATIONS AND RECOMMENDATIONS
JUNE 30, 2008

Mgt. Hr.
7/10/09



SIMPSON & SIMPSON
CERTIFIED PUBLIC ACCOUNTANTS

FOUNDING PARTNERS
BRINARD C. SIMPSON, CPA
CARL P. SIMPSON, CPA

3600 WILSHIRE BOULEVARD, SUITE 1710
LOS ANGELES, CA 90010
(213) 736-6664 TELEPHONE
(213) 736-6692 FAX
www.simpsonandsimpsoncpas.com

December 30, 2008

*Honorable Members of the City Council
City of Los Angeles, California*

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Los Angeles, California (City) as of and for the year ended June 30, 2008, which collectively comprise the City's basic financial statements and have issued our report thereon dated December 30, 2008. Our report was modified to include a reference to other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the entity's internal control over financial reporting. We have issued our Independent Auditor's Report on Internal Control over Financial Reporting and Compliance and Other Matters, which is dated December 30, 2008; Independent Auditor's Report on Compliance with Requirements Applicable to each Major Federal Program and on Internal Control over Compliance, which is dated February 20, 2009; and Schedule of Findings and Questioned Costs, which is dated February 20, 2009. Disclosures in those reports and schedule should be considered in conjunction with this management letter.

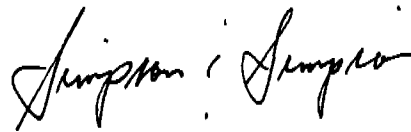
During our audit, we noted several deficiencies in the internal control over financial reporting that we considered to be significant deficiencies and a significant deficiency that we considered to be a material weakness, that are reported in the "Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on An Audit of The Financial Statements Performed in Accordance with *Government Auditing Standards*" dated December 30, 2008.

We also noted certain matters involving the internal control structure that are presented herewith for your consideration. Our observations and recommendations have been discussed with appropriate members of management and are intended to improve the internal control structure or result in operating efficiencies. This letter does not affect the report dated December 30, 2008 on the financial statements of the City.

This report is intended solely for the information and use of the City Council, City Controller, management of the City, and its regulatory agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Thank you for the opportunity to serve the City. We appreciate the courtesy and cooperation extended to us during our audit.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Simpson & Simpson", written in dark ink.

Simpson & Simpson

CITY OF LOS ANGELES, CALIFORNIA

OBSERVATIONS AND RECOMMENDATIONS
JUNE 30, 2008

2008-1. Develop Written Policies and Procedures for the Calculation of Allowance for Uncollectibles for Business Taxes

Condition

During our testing of the allowance for uncollectibles for business taxes, we noted that the City did not have written policies and procedures to document the methodology for estimating the allowance for uncollectibles for business taxes. Also, the City did not maintain centralized and comprehensive data to support the calculation.

Recommendation

We recommend that the Office of Finance develop written policies and procedures to document the methodology and maintain supporting data and detail worksheets for the calculation of allowance for uncollectibles for business taxes. The Office of Finance should also ensure that the written policies and procedures are consistently applied and the calculation worksheets be reviewed.

Management's Response

In the estimation of the allowance for uncollectibles for business taxes, we factored a "valuation allowance" in accordance with generally accepted accounting principles to account for the estimated tax assessments and more accurately reflect the true value of the taxes receivable. We agree that written policies and procedures should be developed and consistently applied, and will provide supporting data for the calculation of the allowance for uncollectible business taxes.

CITY OF LOS ANGELES, CALIFORNIA

OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2008-2. Improve Loan Recording Process at the Housing Department

Condition

We noted that a loan disbursed at the end of fiscal year 2007-08 was not recorded timely by the Housing Department (LAHD) into the Loan Tracking System (LTS). The loan was entered into the LTS in February 2009. Since this is a forgivable loan, the net realizable loan receivable amount is not considered material to the government-wide financial statements.

According to the management of the LAHD, the reason for the above condition was due to the delay in reviewing and approving the loan package and eventually assigning a loan tracking number to the loan.

Recommendation

We recommend that the LAHD streamline the loan recording process and improve communication and document flow to ensure that a new loan will be entered into the system in a timely manner.

Management's Response

When the loan servicing system was designed, it was intended to service real estate secured loans, which represent virtually all of the department's portfolio. However, the loan discussed above is an unsecured forgivable loan that finances a loss reserve for the New Generation Fund, which is the first of this type of a loan for the Department. For this reason, set up for this unsecured loan presented unforeseen problems as it could not follow the normal process for setting up a real estate loan when the system was designed.

Due to timing issues, the loan for the New Generation Fund was disbursed first and was not set up until it was determined whether and how this unsecured loan should be set up in the system. This is not the Department's operating procedure for real estate loans, which requires that loans must be first set up in the servicing system prior to any disbursements being made. For all future project disbursements, accounting will confirm with program management to determine if they are loan related, and if they are, ensure that the related loan is set up in the system prior to releasing disbursements.

CITY OF LOS ANGELES, CALIFORNIA

OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2008-3. Implement Procedures to Resolve the Difference in Investment Balance between Cash Control and SYMPRO

Condition

There is a difference in the General Pool investment balance in the amount of \$460,821 between Cash Control and SYMPRO, the Office of the Treasurer's investment management system, as of June 30, 2008. The Office of the Treasurer identified that the difference was caused by the following two reasons:

- (1) SYMPRO's inability to accommodate the in-house transfer of investments from the reserve (long-term) portfolio to the core (short-term) portfolio. As a result, the in-house transfer transactions were recorded as a sale entry for removing (transferring out) the investment from the reserve portfolio and a purchase entry for adding (transferring in) the investment to the core portfolio in SYMPRO. SYMPRO automatically recognized accrued purchase interest for the investment purchase entry, which was not applicable for the in-house transfer. As a result, the investment balance per SYMPRO is overstated by \$457,824.
- (2) Errors in Cash Receipt (CR) entries for investment income receipts from mortgage backed securities (MBS) and collateralized mortgage obligations (CMO). SYMPRO is designed to manage fixed-income investments which normally pay only interest income to investors semi-annually based on the quoted rate on the face value until maturity. However, MBS and CMO normally pay both principal and interest monthly to their investors. Due to the difference in investment payment structures, SYMPRO was not able to provide accurate information for CR entries. In addition, there were errors in CR entries for investments sold prior to the first interest payment date. As a result, the investment balance per Cash Control is overstated by \$918,645.

Recommendation

We recommend that the City Treasury Office resolve the difference between Cash Control and SYMPRO and implement additional control procedures to properly record and report transactions for in-house investment transfers and MBS/CMO investments.

CITY OF LOS ANGELES, CALIFORNIA

OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

- 2008-3. Implement Procedures to Resolve the Difference in Investment Balance between Cash Control and SYMPRO (Continued)

Management's Response

The Office of the Treasurer has taken actions to implement the recommendation. The difference between SYMPRO and Cash Control in the amount of \$457,824 was resolved when these transferred investments matured in the first quarter of 2009. In addition, correction entries for the errors noted in the CR described in item (2) were recorded in cash control and FMIS. The Office of the Treasurer has also requested a budget appropriation so that the present Cash Control spreadsheet can be replaced with a more efficient system.

CITY OF LOS ANGELES, CALIFORNIA

OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2008-4. Use Appropriate Worksheet to Properly Recognize and Report State Mandated Program Receivable

Condition

The LAPD uses a summary worksheet to track claim billings and payments received for a State Mandated program. The outstanding amount shown on the worksheet was used for the recording of the State Mandated program receivables and reported as part of the intergovernmental receivable in the City's annual financial statements.

Based on our testing of the summary worksheet, we noted that the outstanding amount was understated by approximately \$1.6 million due to the inclusion of estimated revenue receipts in the summary worksheet. As a result, the intergovernmental receivable was understated. The LAPD indicated that the worksheet was originally designed for management and budgeting purposes and was subsequently used for the financial accounting and reporting purposes.

Recommendation

We recommend that the LAPD design a worksheet to properly recognize claim billings, payments received, and outstanding amount of the State Mandated program to meet the requirement for financial accounting and reporting in accordance with generally accepted accounting principles.

Management's Response

LAPD will redesign the worksheet to properly recognize the claim billings, payments received, and outstanding amount of the State Mandated program.

CITY OF LOS ANGELES, CALIFORNIA

**STATUS OF PRIOR YEARS' OBSERVATIONS AND RECOMMENDATIONS
JUNE 30, 2008**

2007-1. Strengthen Controls Over Calculation of Allowance for Uncollectibles for Parking Citations Receivable

Condition

Los Angeles Department of Transportation (LADOT) engaged an outside contractor for parking citations collection services. On a monthly basis, the outside contractor provides to LADOT a summary report on the collection progress including the number of citations issued, amount collected, amount disputed, and uncollectible amounts. LADOT's staff manually transfers data on the monthly report to a worksheet that calculates the allowance for uncollectible accounts.

During our audit of parking citations receivable, we noted that the allowance for uncollectibles as of June 30, 2007 was understated by \$1.5 million. LADOT's staff incorrectly transferred certain information on the monthly report to the worksheet used for the calculation of the allowance.

Recommendation

We recommend that LADOT strengthen controls over calculation of allowance for uncollectibles for parking citations receivable by streamlining the process to detect errors from manual entries and ensuring proper review of the calculation by a supervisor.

Management's Response

LADOT will request an electronic version of the monthly report from the outside contractor to avoid any manual entry error. LADOT will ensure that a supervisor properly reviews the calculation.

Current Year Status

The recommendation has been implemented. The calculation of allowance for uncollectibles for parking citations receivable has been streamlined and properly reviewed by a supervisor.

CITY OF LOS ANGELES, CALIFORNIA

STATUS OF PRIOR YEARS' OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2007-2. Ensure Timeliness of Recording Loan Transfers

Condition

The Mayor and Council, through Council File No. 94-2120, directed that six service repayment loans with a total outstanding balance of \$4,103,309 be transferred from the Los Angeles Housing Department (LAHD) to the Los Angeles Community Development Department (CDD). As of June 30, 2007, LAHD has removed the subject loans from its portfolio. However, based on our review of CDD's loan receivable records, only three loans totaling \$2,607,521 were recorded in CDD's tracking system. The remaining three loans of \$1,495,788 were not included in CDD's tracking system and were therefore excluded in the City's loans receivable balance. This resulted in an audit adjustment.

According to CDD's management, there was a delay in verifying and validating the loans that were transferred from LAHD due to limited staffing resources.

Recommendation

We recommend that the City update its loan tracking systems in a timely manner.

Management's Response

CDD agreed with the audit adjustment. CDD has recorded one of three remaining loans in its portfolio. The rest of transferred loans will be included in CDD's portfolio by June 30, 2008.

Current Year Status

The recommendation has been implemented. These transferred loans have been included in the CDD's portfolio.

CITY OF LOS ANGELES, CALIFORNIA

STATUS OF PRIOR YEARS' OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2007-3. Develop Written Policies and Procedures for Billing, Processing, and Reporting of False Alarm Fees

Condition

Based on our tests, the false alarm fees receivable balance of \$13.5 million at June 30, 2007 was overstated by \$2.8 million. We noted that there are no formal policies and procedures for recording false alarm fees receivable. The False Alarm Section (FAS) of the Los Angeles Police Department (LAPD) utilizes the Office of Finance's financial management system, LATAX, for billing and collection of false alarm fees. LATAX is maintained by Information Technology Agency (ITA). At the end of the fiscal year, LAPD's Fiscal Operation Division (FOD) reports the false alarm fees receivable and allowance for uncollectibles to the Controller's Office which are based on a summary report generated from LATAX. Our review of the summary report indicated that the parameters (i.e., aging of receivables) were not defined and the report was not reviewed for accuracy.

Recommendation

We recommend that LAPD develop written policies and procedures for processing, billing, and reporting of false alarm fees. Also, the policies and procedures should include supervisory review and approval.

Management's Response

LAPD has taken actions to improve the policies and procedures for billing, processing, and reporting of false alarm fees. LAPD has developed a manual which outlines the policies and procedures for processing, billing, and reporting of false alarm fees. Currently, LAPD is working with ITA and Office of Finance to generate the necessary reports for financial reporting. In addition, LAPD is in the final process of recommending the procurement of a new false alarm and permit management system. The current manual will be updated as the new system is developed and implemented.

Current Year Status

LAPD entered an agreement with a professional service company for a new alarm and permit management system in August 2008. The new system will provide a variety of services, including permit tracking, status changes, data interface, false alarm correspondence, billing, and accounts receivable management. The system will interface with the City's tax and permit system (LATAX) to improve the efficiency of billing, recording, and reporting of false alarm fees.

CITY OF LOS ANGELES, CALIFORNIA

STATUS OF PRIOR YEARS' OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2007-3. Develop Written Policies and Procedures for Billing, Processing, and Reporting of False Alarm Fees (Continued)

The implementation of the new system is currently in the Acceptance Test Plan phase. LAPD will validate the operation of the new system and the interfaces with LATAX and LAPD's dispatching system. The new system is scheduled to go live on June 15, 2009.

The current procedures manual is being revised to incorporate changes in policies and procedures related to business practices of the False Alarm Section, including the procedures for billing, processing, and reporting of false alarm fees. The revised manual is expected to be finalized by June 30, 2009.

CITY OF LOS ANGELES, CALIFORNIA

STATUS OF PRIOR YEARS' OBSERVATIONS AND RECOMMENDATIONS

JUNE 30, 2008

(Continued)

2003-3. Timely Reporting by the Enterprise Departments, Component Unit, and Pension Plans

Condition

Each year, the City Controller requests copies of the audited financial statements and certain schedules from the City's proprietary funds, component unit, and pension plans to be submitted by mid-November. However, during the June 30, 2003 reporting year, we noted that the enterprise departments, component unit, and pension plans were non-responsive to the City's financial reporting deadline. The audited financial statements and related schedules of the proprietary funds, component unit, and pension plans were provided to the Controller's Office in late December, causing the delay in the issuance of the City's Comprehensive Annual Financial Report (CAFR). In order to be considered timely, current reporting standards require that annual financial statements should be issued within six months of the close of the fiscal year. The City's CAFR for the fiscal year ended June 30, 2003 was issued on January 20, 2004.

Recommendation

We recommend City management to effectively communicate to the aforementioned entities' management, the importance of the timely submission of the entities' audited financial statements to the City Controller. The City, as a whole, has the fiduciary responsibility to report to its stakeholders, in a timely manner, its financial condition and results of operations.

We also encourage the Mayor, the Controller, and the City Council to take appropriate measures to ensure the aforementioned entities' compliance with the City's financial reporting requirements.

Current Year Status

The volatile financial market condition in the second half of 2008 has resulted in an increased emphasis on the review of post balance sheet date events for the impact of the high-risk financial conditions on the City's pension plans' and proprietary departments' financial statements. The City and its external auditors, including the external auditors of the separately audited component units, expanded work on subsequent events related to the cash and investment accounts for the fiscal year ended June 30, 2008, causing the delay in the issuance of the City's CAFR.

The City's CAFR for the fiscal year ended June 30, 2008 was dated December 30, 2008 and submitted to the Government Finance Officers Association (GFOA) on January 29, 2009.